Hearing on FY 2003 Appropriations

U.S. House of Representatives Subcommittee on VA, HUD, and Independent Agencies

Written Statement

Tony T. Brown, Director

DEPARTMENT OF THE TREASURY
Community Development Financial
Institutions Fund

March 14, 2002



COMMUNITY
DEVELOPMENT
FINANCIAL
INSTITUTIONS
(CDFI) FUND



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INTRODUCTION

Chairman Walsh, Congressman Mollohan and Members of the Subcommittee, I appreciate the opportunity to testify before you today on behalf of the Department of Treasury's Community Development Financial Institutions (CDFI) Fund and in support of the President's FY 2003 budget. I am Tony Brown, the new Director of the CDFI Fund. The Secretary of the Treasury selected me as Director in August of last year. I bring a 20-year prior experience in banking to the CDFI Fund with a decade of service in community development where I managed the community development program for the largest financial institution in the State of Florida. Joining me today are Fred Cooper, Deputy Director for Policy and Programs, and Owen Jones, Deputy Director for Management/CFO.

As you know, the CDFI Fund is a wholly owned government corporation within the United States Department of the Treasury. The Fund promotes access to capital and local economic growth by directly investing in and supporting community development financial institutions (CDFIs) that provide loans, investments, financial services and technical assistance to underserved people and economically distressed communities. CDFIs are specialized financial institutions operating in market niches that have not been adequately served by traditional financial institutions. Included in the various types of CDFIs are community development banks, credit unions, business loan funds, housing/facilities loan funds, microenterprise loan funds, and venture capital funds. As of February 15, 2002, the Fund has certified 553 institutions as CDFIs. These CDFIs operate in all 50 states.

Our vision for the CDFI Fund is to become a leading vehicle and the best practice government agency for financing economic and community development activities in low-income areas to improve the standard of living for Americans living in distressed and underserved communities. Our goal is to help make America a place where all of its

people, including those in such communities, have access to affordable credit, capital and financial services so that they too can realize the American dream. We characterize FY 2003 as a transition year where the Fund shifts from an organization seen primarily as a grants-making organization to one that addresses the economic ills of low-income communities through targeted investments and community development finance.

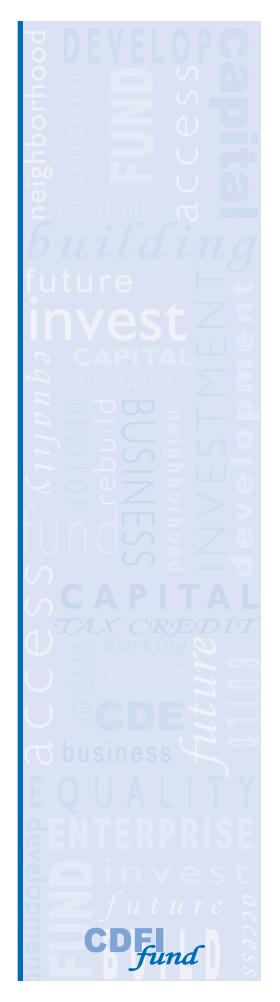
By so doing we will help the Department of Treasury achieve its economic mission of a prosperous and stable America. This ambitious undertaking is explained in this testimony.

My testimony will focus on four key areas: the performance of the CDFI Fund in 2003 and beyond; the President's FY 2003 budget; management and operations; and CDFI Fund programs.

PERFORMANCE OF THE CDFI FUND: 2003 AND BEYOND

Treasury Secretary O'Neill has challenged all employees of the Department to make the Treasury a world-class organization. Additionally, he has instructed the CDFI Fund to develop procedures to provide a meaningful measurement of the impact and results of taxpayer dollars awarded through CDFI Fund programs. In order to successfully work toward the goals set by the Secretary, I have asked CDFI Fund staff to help me establish the CDFI Fund as a leading vehicle for the delivery of community development finance, capital and service activities within the federal government as well as in the nation, so that we have a demonstrable impact on low-income communities. I envision the CDFI Fund becoming an "expert" source in this regard.

As we reported last year, Treasury Secretary O'Neill intends that performance measures of the CDFI Fund and all Treasury activities be more useful and relevant to the decision-making process, and improve the timeliness and accuracy of the information systems that capture and report performance data. To move forward on this commitment, the Secretary has called for a fundamental review within all Treasury bureaus of what we do and why we do it, resulting in a determination of what measures of outputs and outcomes best capture what we are trying to achieve. This points out the need for consistent ways to evaluate the effectiveness of the various incentives for investment in low-income communities so that we have a better understanding of what works and what does not work. The CDFI Fund is committed to working with the Secretary in this important initiative. Our budget includes \$500,000 in additional administrative funding so that we can collect loan-level data to report performance and impact of CDFI activities similar to the administration of the Community Reinvestment Act and the Home Mortgage Disclosure Act.





This initiative will, I believe, enable us to measure the types of impact of our funding that Secretary O'Neill is seeking. The CDFI Fund is working with the community development industry to build a set of performance measures and establish a "performance matrix" for our awardees. This matrix will rate financial stability and community development impact. By using financial and economic factors, we intend to assess how CDFIs improve economic conditions of communities that are underserved by traditional financial institutions.

Our plan is to use this rating system to better manage the CDFI Fund's portfolio of investments and to identify under performing entities and create a compliance "watch list." We believe a significant investment to collect and analyze loan-level data will enhance our ability to report impact in various forms. These initiatives will be incorporated into the CDFI Data Project, making that industry-wide data collection effort even more useful to the CDFI Fund and others interested in CDFIs.

Turning to the impact that CDFI Fund awardees are having in their communities, the CDFI Fund is keenly interested in the issue of impact and how it is measured. The Fund is on the forefront of improving data collection and reporting in the CDFI industry and is one of the founders of the CDFI Data Project (CDP), a collaborative effort of 13 entities — including the Ford and MacArthur Foundations and the six major CDFI trade associations — to develop a standardized data collection system for the CDFI industry. The goal of the CDP is to produce comprehensive, high-quality activity and performance data on CDFIs. The CDFI Fund and other CDP participants issued their first collaborative annual survey last spring; selective results for CDFI awardees are described below.

Measuring community development impact has been a challenge to the CDFI Fund and the industry overall. The General Accounting Office (GAO) recognized this in its 1998 report, entitled "CDFI Fund Needs Better Systems to Measure, Monitor, and Evaluate Awardees' Performance." In the next two years, the CDFI Fund increasingly will focus on identifying additional measures of impact. For example, the Fund has begun an initiative to collect loan-level data from CDFIs. This data will show exactly where CDFIs are lending relative to more traditional lenders and thus give us a better idea of the role CDFIs play in filling the gap in affordable financial services. The MacArthur Foundation has embraced this initiative, and the CDP has incorporated loan-level data collection as well as broader impact measurement research into its strategic plan.

Internally, the CDFI Fund is reviewing the way we collect outcome information from our awardees. To date, each awardee's performance goals and measures have been tailored to their specific activities. While these measures were rich in their uniqueness, the outcomes they measured could not be aggregated across CDFIs because they were not comparable. The CDFI Fund plans to revise its awardee performance goal and measurement system so that it produces stan-

dardized information on all CDFIs. To the extent possible, we will incorporate the CDFI Fund's reporting requirements in the annual survey in order to minimize reporting burdens on CDFIs and facilitate data analysis at the Fund.

Finally, the CDFI Fund is beginning to conduct peer analyses in an effort to develop industry performance benchmarks for each type of CDFI. We will use this information to "risk rate" our portfolio of awardees. Once it is tested and proven, we will consider other uses such as incorporating it into our award decision-making process. All of these efforts respond to findings and recommendations in the 1998 GAO report.

It is incumbent upon the CDFI Fund to continually improve its processes and develop a system for accurately measuring the real impact of CDFI Fund dollars in the communities served by our customers.

PRESIDENT'S FY 2003 BUDGET

The President's FY 2003 budget requests \$68 million in appropriations for the CDFI Fund. This is the same funding level as requested in last year's Presidential budget. The Administration request should be considered in light of several factors.

First, the proposed budget for the CDFI Fund reflects overall federal budget priorities for increased National Security and Homeland Security.

Second, the FY 2003 budget level of \$68 million maintains a basic level of funding to support CDFI Fund programs and assumes significant improvements in how we process applications. To do this we hope to successfully streamline our award approval and disbursement processes. We believe substantial savings in staff time will occur through streamlined efforts. This will enable us to provide the much needed community development capital to qualifying organizations with a quicker disbursement of funds for those organizations who meet all program criteria at the date of application.

Third, the enactment of the Community Renewal Tax Relief Act of 2000 will devote substantial additional resources to new incentives for investment in low-income communities. This includes the New Markets Tax Credit (NMTC) Program, to be administered by the CDFI Fund. The NMTC Program is a new and, we believe, an exciting program for the CDFI Fund. The NMTCs are expected to generate \$15 billion in investments in low-income communities over the next seven years. We are working diligently to allocate credits this year and measure their impact in FY 2003, or as quickly as these credits are used, as an incentive to attract equity capital. Although the allocations for NMTCs are expected to be announced in the fall of calendar





year 2002, we may not see the effect of the NMTC- leveraged equity investments in low-income communities before calendar year 2004. Obviously, the first year of this program will be a work in progress since we have a limited sense of the demand or actual appetite of investors for these types of tax credit allocations. The successful implementation of the NMTC Program is one of our highest priorities. The NMTC Program offers us a unique opportunity to measure the increased flow of private capital into low-income communities. Our resources are mobilized to ensure a successful introduction of the NMTC Program this calendar year.

Lastly, we anticipate that approximately \$30 million of the proposed FY 2003 budget will be used to fund the Core and Intermediary Components of the CDFI Program and Training Program; approximately \$9 million will be made available for the Small and Emerging CDFI Assistance (SECA) and the Native American CDFI Technical Assistance (NACTA) Components of the CDFI Program; and \$20 million will be used to fund the Bank Enterprise Award (BEA) Program. The remainder will be used to cover the CDFI Fund's administrative costs, including the costs of administering the NMTC Program.

The CDFI Fund will continue to focus efforts on serving those markets, including rural and Native American communities, that have relatively low levels of CDFI activity and inadequate access to financial services. In these areas, we will continue to conduct workshops (both in-person and via satellite broadcasts) detailing the CDFI certification and funding application processes. We also expect that the SECA Component, the NACTA Component, and the Training Program will be of particular benefit to CDFIs and CDFIs in formation that serve these difficult markets.

MANAGEMENT AND OPERATIONS

The CDFI Fund has implemented effective financial and management controls as verified by our independent auditors (KPMG, LLP). These controls have allowed the CDFI Fund, for the fifth consecutive year, to receive an unqualified (clean) audit opinion. Additionally, this marks the fourth consecutive year that the independent auditors have identified no material weaknesses or reportable conditions. KPMG's opinion affirms the CDFI Fund's Statements of Financial Position, Operations, and Changes in Net Position and Cash Flow are fairly presented. These findings reflect the commitment of the CDFI Fund to sustaining and improving upon its internal controls, operating policy and procedures, and awards management.

The CDFI Fund continues to comply with the Federal Managers' Financial Integrity Act (FMFIA) and the Federal Financial Management Improvement Act (FFMIA). The CDFI Fund's system of internal management, accounting and administrative controls are operating effectively.

During my seven months as Director, I have spent a significant amount of time reviewing the internal operations at the CDFI Fund. It is my intention to make necessary changes, which will streamline and make more efficient our processes and procedures. It is my hope that, once implemented, these changes will accomplish four key goals. First, as mentioned above, we need to reduce the amount of time currently required for our award processes. This includes reducing time used for application reviews, awards obligation and disbursement of funds. Second, our plan will successfully integrate the NMTC Program within our existing operations without significantly increasing the number of new employees above FY 2002 levels. Third, we need to enhance the CDFI Fund's ability to perform research, market and portfolio analysis to measure the availability of financial services in underserved markets and critique the financial and program performance of existing CDFIs. Finally, I want to position the CDFI Fund to be better prepared and anticipate future responsibilities.

CDFI FUND PROGRAMS

The CDFI Fund supports its economic development mission of providing capital to underserved persons and in underserved markets by investing in CDFIs, and by providing incentives for mainstream financial institutions to invest in CDFIs and increase their activities in distressed communities. In addition to three traditional programs (the CDFI Program, the Bank Enterprise Award (BEA) Program, and the Training Program), the CDFI Fund has introduced two new programs. We anticipate these programs will provide additional capital in the markets served by our customers. These new programs are the New Markets Tax Credit (NMTC) Program, described above, and the Native American CDFI Technical Assistance (NACTA) Component of the CDFI Program.

CDFI Program

The CDFI Program provides financial assistance in the form of grants, loans, equity investments or deposits to CDFIs. Since its inception, the CDFI Fund has made over 780 CDFI Program awards totaling \$357 million. The CDFI Program is composed of three separate funding components, each attempting to reach a different type of CDFI or market: the Core Component; the Small and Emerging CDFI Assistance (SECA) Component (formerly the Technical Assistance Component); and the NACTA Component.

CDFIs also provide their clients with training and technical assistance that help organizational clients to better manage community development projects and help individual clients to improve their financial decision-making skills and increase their options for accessing credit. This type of borrower education is the foundation for mitigating losses in the CDFI industry overall. In FY 2000, the CDFI Fund's awardees provided business training, financial management education, credit





counseling, and homebuyer training to 51,059 individuals and 6,298 non-profits and other organizations.

In addition to financing activities, CDFIs are also depository institutions; 159 of the 553 certified CDFIs are regulated financial institutions (banks, thrifts, and credit unions). In a survey completed in 2000, 21 depository awardees—primarily low-income designated credit unions and community development banks — provided 141,440 checking and savings accounts, with \$257 million on deposit for an average of \$1,815 per account. Each of these institutions has a mission of reaching low-income and underserved populations, and some provide products specifically designed to help low-income individuals build wealth, such as Individual Development Accounts. In all, 985 Individual Development Accounts held savings of \$388,545, an average of \$395 per low-income account holder.

Finally, CDFI Fund awardees have leveraged significant additional capital. A sample of non-depository CDFIs estimated that they were able to raise an additional \$69 million over and above the required 1:1 match due to being a CDFI Fund awardee or certified CDFI, representing an additional \$1.48 raised for every CDFI Fund award dollar. This capital has come from banks, foundations, state and local government, and others.1

The Core Component is directed at building the financial capacity of CDFIs by enhancing the capital base. Awardees of the Core Component represent some of the nation's largest loan funds and financial institutions. At the end of FY 2000, 122 Core awardees reported \$2 billion in outstanding loans and investments.

In FY 2001, the CDFI Fund provided 51 Core Component awards totaling \$48 million. These 51 awardees are based in 27 states. There are now CDFI Program awardees in 49 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands. Of these 51 awardees, 10 have multi-state or national service areas; 38 serve rural markets.

In addition to geographic diversity, the types of CDFIs assisted and the array of loan or investment products provided is broad: 26 provide loans for housing development or ownership; 20 have micro- or small-business loan products; five are credit unions; three are community development bank holding companies; and two are venture capital funds.

Entities selected for Core Component awards typically have business strategies that support economic stabilization or building wealth in low-wealth markets. A few examples include:

Homeward Inc. of Allison, Iowa, was formed out of a consortium of eight rural electric cooperatives to provide loans for housing development and for economic development activities.

Home Headquarters of Syracuse, NY helps to stabilize distressed neighborhoods and build assets in Onondaga County through home purchase financing targeted to lower income households.

Kentucky Highlands Investment Corporation is a nonprofit business development firm founded in 1968 to provide venture capital and debt financing to start-up and expanding businesses. In a nine-county region of Appalachia, Kentucky Highlands, through its financial products, has helped to create or retain 7,000 jobs. This means that, on average, 12 percent of the households in this rural nine-county region have a family member employed by a company that Kentucky Highlands assisted. In the local Empowerment Zone, which is located within the nine-county region, this CDFI's impact is even greater: since 1994, Kentucky Highlands helped create or retain 3,086 jobs in the area that is now part of the Empowerment Zone. This translates into an average of 39.7 percent of EZ households with a family member employed by a company that Kentucky Highlands helped.

On September 24, 2001, the CDFI Fund published a Notice of Funds Availability (NOFA) announcing the availability of \$36.9 million in Core Component awards for FY 2002. The application deadline was December 11, 2001; we received 136 applications, requesting a total of \$198 million.

The Intermediary Component allows the CDFI Fund to invest in CDFIs through intermediary organizations that support other CDFIs and emerging CDFIs. These intermediary entities, which are also CDFIs, generally provide financial and technical assistance to small and growing CDFIs. Like Core awardees, Intermediary awardees are required to obtain matching funds in comparable form and value to the financial assistance they receive from the CDFI Fund.

Since inception, the CDFI Fund has obligated awards totaling over \$20 million to 11 different intermediary institutions. Beginning with the FY 2001 funding round, the Intermediary Component has been announced and evaluated as part of the Core Component and CDFI Intermediaries now compete directly with other Core Program applicants.

The Small and Emerging CDFI Assistance (SECA) Component was initiated in FY 2001. It replaces the Technical Assistance (TA) Component, which was first introduced in 1998 to build the capacity of CDFIs to serve their target markets—- particularly "start-up," young and small institutions. Under the TA Component, the CDFI Fund directed relatively small amounts of funds — generally \$50,000 or less — to CDFIs that could demonstrate significant potential for generating community development impact, but whose institutional capacity needed to be strengthened in order to fully realize this potential. Some typical uses of TA grants included: computer system upgrades and software acquisition; developing loan underwriting policies and procedures; evaluating current loan products and developing new ones; and training staff. Under the SECA Component, the CDFI Fund





has augmented the range of assistance provided under the predecessor TA Component. In addition to TA grants, eligible applicants can also request Financial Assistance, generally used for enhancing the applicant's lending capital, up to \$150,000. Small and emerging CDFIs generally have less than \$5 million in assets and have never received Financial Assistance from the CDFI Fund. Requests for Financial Assistance must be matched dollar-for-dollar with other non-Federal funds.

In FY 2001, the Fund provided 70 SECA/TA Component awards totaling \$8 million. Of the FY 2001 awardees, 26 (32 percent) are startups. We are pleased to report that the SECA Component has been particularly responsive to the needs of community development credit unions: 20 (or almost 30 percent) of the FY 2001 SECA awardees are credit unions. The SECA Component also has proved to have national reach: the 70 SECA awardees are located in 26 states, Washington, D.C., and Puerto Rico. Of these 70 awardees, about half (37) include rural markets within their service areas.

On September 24, 2001, the CDFI Fund published a NOFA announcing the availability of \$5.6 million under the SECA Component for FY 2002. A total of 120 applications was received, for \$18 million.

SECA Component awardees are serving some of the nation's most economically distressed and hardest to serve markets and are exhibiting important programmatic innovations. The CDFI Fund's SECA Component awards are helping to build the organizational infrastructure to increase the flow of capital in economically distressed areas and to low-wealth populations:

The Bushwick Federal Credit Union is a recently chartered start-up serving the economically distressed Bushwick neighborhood of Brooklyn, New York. It provides financially literacy to a largely unbanked population. It proposes to use its award to capitalize a micro loan product and to expand its ATM services.

Nevada Microenterprise Initiative, based in Reno, provides training and financing to lower income entrepreneurs that lack sufficient collateral for conventional financial institutions and proposes to use the award to obtain staff training and to refine its business plan.

Azteca Community Loan Fund of San Juan, Texas, proposes to build its capacity to help build assets among very low-income people through development services and loans that will increase the rate of homeownership in colonias in the south Texas border region.

The Bank Enterprise Award (BEA) Program

The Bank Enterprise Award (BEA) Program is the principal means by which the CDFI Fund achieves its strategic goal of expanding financial service organizations' community development lending and invest-

ments through regulated institutions. The BEA Program recognizes the key role played by mainstream depository institutions in promoting the growth of CDFIs and the revitalization of distressed communities.

The BEA Program provides monetary incentives for banks and thrifts to expand investments in CDFIs and/or to increase lending, investment and service activities in distressed communities. BEA Program awards vary in size, depending upon the type and amount of assistance provided by the bank and the activities being funded through the bank's investments. In general, banks that provide equity investments to CDFIs are likely to receive the largest awards relative to the size of their investments.

Through 2001, 577 BEA Program awards totaling over \$182 million have been provided to banks and thrifts. Banks and thrifts receiving BEA Program awards have provided \$959 million directly to CDFIs, and \$2.5 billion to distressed communities1 in the form of direct loans, investments and services.

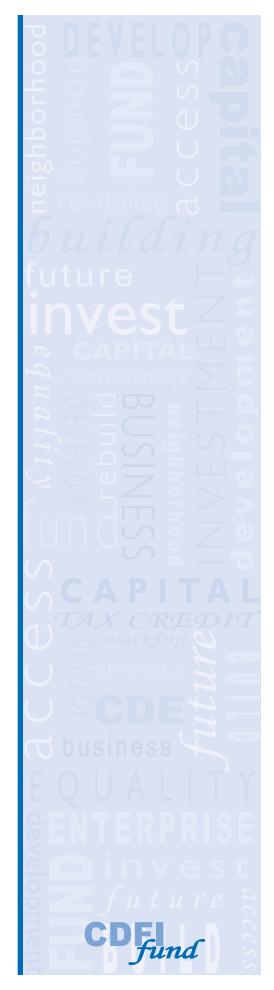
In FY 2001, the CDFI Fund made 139 BEA Program awards totaling \$ 46 million. On September 24, 2001, the CDFI Fund published a NOFA announcing the availability of \$16.5 million in BEA Program funds for FY 2002. The application deadline for this NOFA was November 13, 2001.

The CDFI Fund has made BEA Program awards to 386 different institutions since 1996. The average Total Assets of the 386 BEA Program awardees is just under \$10 billion. BEA Program awardees range in size from \$585 billion in assets to \$8 million. BEA Program awardees have an average Return on Assets of 1.1percent and average Tier One Capital of \$407 million. The BEA Program award as a percentage of Tier One Capital is less than 3 percent on average. All BEA awardees whose BEA Program award represents more then 10 percent of Tier One Capital are certified CDFIs.

All but two BEA Program awardees have Satisfactory or Outstanding Community Reinvestment Act (CRA) ratings. About one-third have Outstanding CRA ratings and about 60 percent have Satisfactory ratings. The BEA Program awardees with Outstanding CRA ratings have an average size (in terms of assets) of \$17 billion, while awardees with Satisfactory Ratings have an average of \$6 billion in Total Assets.

A few examples of BEA Program awardees include:

AmSouth Bank of Birmingham, Alabama received an award of \$221,600 for providing \$300,000 in grants and \$1.6 million in loans to ten CDFIs: Affordable Housing Resources; Community Equity Investments; Enterprise Corporation of the Delta; Florida Community Loan Fund; Local Initiatives Support Corporation; Neighborhood





Housing Services; Southern Development Bancorporation; Nashville Housing Fund; Chattanooga Neighborhood Enterprise; Structured Employment Economic Development Corporation; and Technology 2020 Finance Corporation. The awardee is a state chartered bank with total assets of \$39 billion.

Providian National Bank of Tilton, New Hampshire, received a BEA Program award of \$1,110,000 for making a \$7.5 million equity like loan to the National Community Capital Association, a certified CDFI. Providian's investment will help fund the first national childcare facilities fund, which will provide financial assistance to childcare providers and thereby increase the availability of affordable childcare slots for disadvantaged families and communities in New Hampshire and throughout the country. The awardee is a national bank with total assets of \$15 billion.

Since first participating in the BEA Program in 1996, KeyBank, a national bank based in Cleveland, Ohio, has received a total of \$2.3 million for providing over \$22 million in financial support (including grant, equity-like loans, and loans) to several CDFIs: Cascadia Revolving Loan Fund, Coastal Enterprises, Coastal Ventures Limited Partnership, Coastal Ventures II, LLC, Cincinnati Development Fund, Columbus Growth Fund, Community Capital Development, Capital District Loan Fund, Community Preservation Corporation, Denver Neighborhood Housing Fund, The Enterprise Foundation, Funding Partners for Housing Solutions, the Housing Partnership Development Fund, Growth Finance Corporation of Oxford Hills, Housing Partner Development Fund, Impact Capital, Jubilee Community Loan Fund, Local Initiatives Support Corporation, Mutual Financial Services, NHS of Toledo, Northern Community Investment Corporation, Progressive Neighborhood Federal Credit Union, Rural Opportunities Enterprise, Vermont Community Development Loan Fund, and Western Maine Finance. The awardee is a national bank with total assets of \$76 billion.

The Training Program

The Training Program, begun in FY 1999, is aimed at supporting the CDFI Fund's strategic goal of strengthening the organizational capacity and expertise of CDFIs and other Financial Service Organizations. The Training Program provides funds that support the development and delivery of training products to CDFIs and other entities engaged in community development finance. Training is addressed via classroom instruction, web-based distance learning, and other electronic formats. The CDFI Fund is particularly excited about providing the support to help build the electronic teaching capacity of the CDFI industry. Through distance learning, the cost of accessing training is reduced for the CDFIs (elimination of the time and cost of travel) and the ability of CDFIs that are either of limited resources or of remote locations to access training is enhanced.

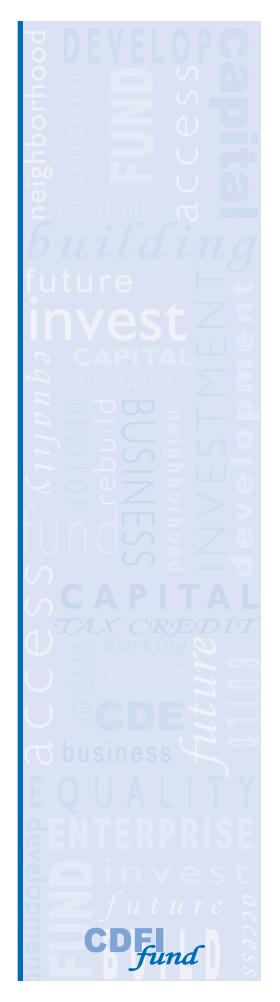
In FY 2001, the CDFI Fund awarded contracts to four training providers for curriculum development and the delivery of three courses: How to Do a Market Analysis; How to Prepare Financial Projections; and How to Develop and Operate a Community Development Lending Program. Training has already begun under each of these courses. Through February 2002, there have been 60 offerings of the three courses supported by the Fund. Each class usually serves up to 30 participants. Through February 2002, it is estimated that 1,200 individuals will have participated in Fund-supported training. Of the four training providers, two providers (the National Community Capital Association and the National Federation of Community Development Credit Unions) are CDFI trade associations. Support to their members and others is provided through advisory services, which is now enhanced through these training products. The CDFI Fund has found these trade associations and other contractors to be good partners in helping to build the capacity of CDFIs in serving their communities — they couple a deep knowledge of the circumstances of the industry with a mission to serve.

New Markets Tax Credit (NMTC) Program

Congress enacted this program in December of 2000 to attract private sector investment in businesses located in low-income communities to improve economic conditions in such communities. Under the NMTC Program, taxpayers will be provided a credit against Federal income taxes for qualified investments made to acquire stock or other equity interests in designated Community Development Entities (CDEs). In turn, substantially all of the proceeds of qualified investments must be used by the CDE to make qualified investments in low-income communities. These qualified low-income community investments include loans to or equity investments in, businesses or CDEs operating in low-income communities. The credit provided to the investor covers a seven-year period. In each of the first three years, the investor receives a credit totaling 5 percent of the total value of the stock or equity interest at the time of purchase. For the final four years, the value of the credit is 6 percent annually.

This calendar year, NMTCs will be allocated annually by the CDFI Fund to for-profit CDEs under a competitive application process. These CDEs in turn will pass the credits to investors (such as banks, corporations, mutual funds, and/or individuals). To qualify for CDE designation by the Fund, an entity must be a domestic corporation or partnership that: (1) has the primary mission of serving, or providing investment capital for low-income communities or low income persons; and (2) maintains accountability to residents of low income communities through representation on a governing or an advisory board.

On April 20, 2001, meeting its statutory mandate, the CDFI Fund issued Guidance relating to the certification of CDEs and the competitive allocation of NMTCs. The Guidance was published in the Federal





Register on May 1, 2001 – the same day that the IRS issued an Advanced Notice of Proposed Rule Making (ANPRM) announcing its intention to develop regulations covering all tax-related aspects of the NMTC Program. Both the Guidance and the ANPRM requested public comments, which were due to the Fund and IRS, respectively, on July 2, 2001. The CDFI Fund received public comments from over 40 different organizations and trade associations.

On December 20, 2001, less than one year after Congress enacted the NMTC Program, the CDFI Fund released application materials enabling organizations to apply to the Fund for designation as CDEs – effectively launching the NMTC Program. The CDFI Fund has fully implemented rules to permit entities to becoming certified CDEs. To date, approximately 175 organizations have been certified as CDEs or currently have CDE applications pending with the CDFI Fund.

The CDFI Fund's objectives for the remainder of the year are to publish an NMTC allocation application, select qualified CDEs to receive an allocation of tax credits, and complete the awards allocation process for 2001/2002 tax credits. The CDFI Fund expects to issue a Notice of Allocation Availability (NOAA) next month announcing the availability of tax credits supporting up to \$2.5 billion worth of equity investments in CDEs. The CDFI Fund will review applications from CDEs under a competitive review process, with the goal of finalizing award decisions by the fall of 2002. In this manner, investors making equity investments into eligible CDEs would be able to claim tax credits during this calendar year.

By offering a tax credit, the NMTC Program encourages private investment in underserved communities. If investors embrace the program, it will be a significant source of new capital that could help to stimulate new industries and entrepreneurs, diversify the local economy, and generate new jobs in low-income communities. Our FY 2003 budget requests \$ 2.7 million in administrative funds to operate this program. This request accounts for 24 percent of our administrative budget.

Native American CDFI Technical Assistance (NACTA) Component

A second recent initiative at the Fund is focused on Native American communities. This initiative includes the Native American CDFI Technical Assistance (NACTA) Component of the CDFI Program and the Native American CDFI Training Program. The CDFI Fund's FY 2001 and 2002 appropriations bills each include a \$5 million set-aside for this effort. The purpose of this initiative is to increase access to capital in Native communities. In response to the set-aside contained in the FY 2001 budget, the Fund issued a Notice of Funds Availability (NOFA) on September 24, 2001, requesting applications under the

NACTA Component. Approximately \$3.5 million of the \$5 million setaside will be available for this round.

The CDFI Fund has received 46 applications for assistance under the NACTA Component. The applications, which are currently under review, represent 21 states. A second NACTA NOFA will draw from the set-aside contained in the FY 2002 CDFI Fund appropriations. Funds will be allocated under the NACTA Component through direct grants to Native CDFIs, Tribal organizations, and other financial institutions and organizations serving these communities. It is anticipated that these funds will: (i) enable financial institutions to enhance their capacity to provide access to capital and credit to these communities; and (ii) assist such communities in establishing their own CDFIs.

Another \$1.5 million of the set-aside is being used to develop a training program. This training program will be designed to help Native American communities build leadership skills enabling them to create and manage CDFIs.

The need for this new initiative was identified during the workshops organized by the CDFI Fund in conjunction with the development of the Native American Lending Study/Action Plan. This Study examines the key barriers to accessing debt capital and equity investments in Native American communities. Numerous actions that could be taken by Tribes, lenders, and local and national policy makers were identified. These ranged from the adoption of the Uniform Commercial Code by Tribal governments to the capacity-building efforts now underway at the CDFI Fund. The final report was distributed in December 2001 to the House and Senate Committees who hold jurisdiction over the CDFI Fund and Native American issues, as well as to the President.

In developing this study, the CDFI Fund conducted 13 regional workshops across the country and two roundtable meetings. The CDFI Fund also administered a national survey of 860 tribal organizations and 750 financial institutions located near Indian reservations, Alaska Native Villages, and Native Hawaiian Communities. The survey collected data such as barriers to accessing capital, accessibility of bank services and products, availability of technical assistance, industrial sector financing gaps and strength of internal tribal resources and policies. The CDFI Fund also administered an equity investment research project to assess the gap and potential opportunities for Native Americans to access this kind of investment.

Rural Community Assistance

Lastly, the FY 2002 appropriations for the CDFI Fund contained report language requesting an update on rural lending practices as part of the fiscal year 2003 budget submission. Core Component and BEA Program awardees are indeed reaching rural areas. Of 123 surveyed Core awardees, 21 (17 percent) estimated that 100 percent of their





activities went to rural areas and an additional 15 (12 percent) estimated that 51 to 99 percent of their activities went to rural areas. Out of 160 surveyed BEA awardees, 11 (7 percent) said that 100 percent of their business activities went to rural areas, and an additional 18 (11 percent) said that 51 to 99 percent of their business went to rural areas. Considering that 22 percent of U.S. households reside in non-metropolitan areas, the percentage of Core awardees that target more than half their activities to rural areas (29 percent) compares favorably, while BEA falls slightly short at 18 percent.

The CDFIs focusing on rural areas tend to be smaller than their urban counterparts and the actual dollar amount that awardees' lend to rural areas is proportionally less than the percent that serve rural areas. An estimated 17 percent (\$351 million) of Core Component awardees' lending and 11 percent (\$161 million) of BEA awardees' lending went to non-metropolitan counties2. The CDFI Fund has identified several options that may increase the flow of CDFI Program and BEA Program awardees' dollars to rural areas. For the BEA Program, the most significant of these would require changes to the Fund's authorizing statute. For example, under the BEA Program, a "distressed area" must have a population of at least 4,000. Distressed areas are composed of census tracts. Many rural census tracts do not have 4,000 people, which in many cases precludes their eligibility as BEA distressed areas. Eliminating the BEA Program population requirement for rural areas would result in more people becoming eligible for consideration under the BEA Program.

In addition, almost all of the new NACTA Component dollars are expected to flow to rural areas: 46 of 47 current NACTA applicants target rural areas.

SUMMARY

Treasury Secretary O'Neill and the Administration have set the bar high for the expected performance from us at Treasury as well as the entire federal government. As you can see, I have laid out a blueprint for the CDFI Fund to enable us to reach goals that will improve and enhance our performance and service to our customers. These goals will hopefully provide an increased efficiency in the use of taxpayer dollars. Our goals are numerous and in some instances, very ambitious. It undoubtedly will require a very focused and conscientious effort by all of us at the CDFI Fund. During my short time at the CDFI Fund, I have developed the utmost confidence in the commitment of our staff toward our customers and the communities that they serve. I am certain that we will all rise to the occasion to meet our goals and do so in a timely and professional manner. I look forward to working with the Members of this Subcommittee towards achieving these goals. Again, I thank you for the opportunity to present my testimony in support of the President's 2003 budget request and look forward to answering any questions you may have for me.

- 1 Source: CDFI Fund FY 2000 Annual Survey of Core Awardees.
- 1 Distressed Community is a defined area that must have a poverty rate of at least 30 percent and an unemployment rate that is at least 1.5 times greater than the national rate.
- 2 Core Component awardee dollar amounts were estimated by applying the awardees' estimated percentage of FY 2000 customers located in rural areas to the awardees' total financing closed in FY 2000. BEA Program awardee dollars were estimated by applying the awardees' estimated percentage of total lending in rural areas to the sum of their total community development and service activities, and CDFI support activities during the BEA assessment period.

